STAFF REPORT

To: Finance Committee Date: March, 2010

Via: Gary Jackson, City Manager

From: Benjamin Durant, Chief Financial Officer

Subject: Montford Commons public/private partnership request

Summary Statement: Policy direction for proposed Montford Commons Public/Private Partnership.

Review: Local Developer Frontier Syndicate has requested approximately $9 million in City/County public financing support to pay for land acquisition and public infrastructure improvements related to their proposed Montford Commons Urban Village project.

To assist with the analysis and evaluation of a potential public/private partnership related to this project, staff engaged an independent advisor to check the references and qualifications of the developer; conduct a market supportability assessment of the project and perform financial gap analysis and review of the project pro-forma. A staff team consisting primarily of Ben Durant, Chief Financial Officer; Bob Oast, City Attorney; and Sam Powers, Economic Development Director, review the RERC's analysis and present the findings outlined below.

Executive Summary

Real Estate Research Consultants (RERC), Inc. was retained by the City of Asheville to conduct the market supportability and financial gap analysis. A copy of RERC's report is attached to this staff report. Key findings, conclusions and other pertinent information drawn from the report are summarized below:

1. Individual equity owners active in the Montford Commons project possess the necessary individual skill sets and qualifications for project planning and development; however, the equity owner's group as an entity has not completed a project to date of similar scope and scale and therefore can not provide project references applicable to the group. Similarly, the ownership group does not have experience nor references for completing projects in which public investments have been made to fill a financial gap; individual owners do possess some experience in this area.

2. RERC concluded that **Phase I** of the Montford Commons project could be viable within the market if developed as proposed. RERC does not believe that there is sufficient commercial/office demand in the area to support **Phases 2 and 3** of the

project. These phases are much more speculative as neither pre-leasing nor equity activities have made any demonstrable progress to date. For planning purposes, the City should assume the commercial portion of the project does not occur.

A summary of the proposed three phases of the Montford Commons project is provided in the chart below:

Phase	Development Program	Construction Duration	Construction Costs
1	275 multifamily for-rent apartments; 6,000 square feet of retail	17 months	$35,000,000
2	22,500 square feet of commercial; 67,500 square feet of office	12 months	$13,261,000
3	16 apartments; 25 single family homes	17 months	$5,332,000

3. The Montford Commons project as currently proposed is a "market-rate" housing project. As such, it does not include an affordable housing component.

   To qualify as "affordable" pursuant to City Housing Trust Fund guidelines, rents must be affordable to households earning 80% or less of median income. The chart below compares the maximum affordable rents for the aforementioned households to the proposed rents in the Montford Commons project:

Type	Affordable Housing Monthly Rents	Montford Commons Proposed Rents
Efficiency /1 Bedroom Flat	$600	$675 - $695
1 Bedroom	$650	$825 - $995
2 Bedroom	$780	$1,050 - $1,150

4. Developer Equity – Frontier Syndicate's current equity contribution to the project is $4.6 million, representing 13% of Phase 1's total construction costs of $35 million. Developers requesting public incentives should have at least 20% equity participation in the project's cost. City support of the project should be conditioned on the developer contributing at least 20% equity in the project in each phase for which incentives are requested.

5. Cash Flow - A review of the cash flow indicated by the developer pro-forma suggests that without some level of public incentive the project as currently conceived is not feasible. RERC, however, does not believe the full amount of incentives requested by Frontier Syndicate is necessary to make the project feasible.

6. Requested Investment

   Frontier Syndicate is currently requesting the following incentives by phase:

Requested Investment	Phase 1	Phase 2	Phase 3	Total
Land Cost	**$600,00**	**$1,000,000**	$0	$1,600,000
Horizontal Improvements	2,905,000 (on-site)	**1,529,000** (offsite)	816,000	5,250.000
Contingencies	330,000	160,000	60,000	550,000
Parking - 117 Spaces	1,404,000	0	0	1,404,000
Total Requested Public Investment	**$5,239,000**	**$2,689,000**	**$876,000**	**$8,804,000**

7. The request for $1,404,000 in public funding for 117 structured parking spaces in Phase 1 is not substantiated as a public cost given the spaces contribute value to a future Phase 2 of the project which currently lacks market supportability.

8. Public financial assistance with the costs associated with land acquisition and off-site horizontal improvements is substantiated subject to the City's goals and objectives for the redevelopment area, budget limitations and competing projects seeking public assistance within the City. Therefore, public assistance in the range of approximately $1.5 million to $3.0 million appears reasonable, subject to the conditions and parameters outlined in RERC's report.

Staff Review

Based on their review of the financial soundness of the Frontier's pro-forma and methodology for calculating a financial gap, RERC concluded that the Montford Commons project has a financial gap. RERC further concluded that the project as currently conceived is not feasible without some level of public assistance. RERC, however, did not provide the exact amount of the gap. RERC felt it would be inappropriate to do so given that Frontier's pro-forma does not reflect actual formal construction cost estimates nor value engineering and includes contingencies, some of which may or may not materialize.

Financial Gap
There are several reasons why a project may show a financing gap (i.e. weak market conditions, high equity requirements, special site conditions that inflate construction costs, etc.) In subsequent consultations with RERC, the consultants suggest that some of the key factors driving the Montford Commons financial gap are land costs and structured parking.

Specifically, Frontier assembled land at the height of the real estate market, which has tended to inflate their development costs. Additionally, Frontier's land acquisition costs included the purchase of a "ravine" for approximately $1.0 million that it planned to package with adjoining property and develop as part of the overall project. The adjoining property, however, is currently owned by a third party that is unwilling to sell. Without the adjoining property, the ravine by itself has low development potential and thus is unlikely to generate project income for Montford Commons.

The inclusion of a $1,404,000 structured parking deck in Phase I of the project is another key contributor to the financial gap. RERC concluded, however, that public funding of the deck is not substantiated as a public cost. The reason is that the spaces contribute value to a future Phase II of the project which currently lacks market supportability, thus presenting a substantial public risk if public financial support were provided. According to RERC, "the117 spaces deck are not required to make the Phase I development feasible nor marketable, and although it may produce economies of scale for the developer, City participation in this cost to guarantee those economies is not merited". RERC concludes that surface parking, rather than a deck, could accommodate Phase I and substantially reduce the project's hard costs and debt service.

Public Assistance

Of the total $8.8 million in financial assistance requested, the consultants concluded that "public assistance in the range of $1.5 to $3.0 appears reasonable subject to the conditions and parameters outlined in RERC's documentation". The minimum of this range of public assistance (i.e. $1.5 million) approximates the project's $1.6 million land acquisition costs, including $1.0 million for the ravine. The assumption behind this suggestion is that if the City purchased the ravine, the city could assist in reducing Frontier's development costs, and in turn the City would acquire a piece of property that could be used for preservation of green/open space and subsequent greenway development. This purchase, of course, is subject to Council policy objectives.

The top end of the suggested range of public assistance ($3.0 million) is calculated by adding approximately $1.5 million of projected off-site infrastructure costs to the preceding land acquisitions costs. The off-site infrastructure costs include the following:

• Roadways	$1,186,000
• Water Lines	42,900
• Sanitary Sewer	41,520
• Erosion/Sediment Control	70,000
• Greenway Path	50,000
• Contingencies	139,042
Total	$1,529,000

Potential city participation in offsite infrastructure costs is based on the assumption that offsite infrastructure improvements can produce system-wide benefits. That is, they produce general public purpose benefits that the public at large can enjoy or that can spur future development. Conversely, on-site improvements typically produce direct benefits for the developer and thus are absorbed in their cost of construction.

Based on staff's review of the offsite costs, it is clear that some costs have more of benefit to the general public than others. For instance, included in the $1.19 million of roadway improvements is $500,000 (City Transportation Department staff estimates this cost to be closer to $250,000) to upgrade the traffic signal system at the intersection of Montford Avenue and Cherry Street and Montford Avenue and Haywood Street. Improvements at these intersections are already a high priority for the Transportation Department because congestion issues currently exist during the weekday morning and afternoon peak hours; thus, partnering with the developer to upgrade the signal system may be good for the City.

Not all of the offsite improvements, however, are "essential" to the project; nor do they produce system-wide benefits. As such, justification for City participation in these costs is less clear. The $1.19 million in the roadway costs total, for instance, also includes $400,000 to widen Hill Street and $250,000 to construct a road that connects the Chamber of Commerce to the Montford Commons development. According to the City traffic engineer, the widening of Hill Street is only necessary if full development of the project occurs, thus the cost and benefit is tied directly to the project. Further, according to Frontier Syndicate, the chamber road connection, while a nice amenity, is a non-essential aspect of the project.

As previously stated, on-site improvements produce direct benefits for the developer and thus are typically absorbed in the developer's cost of construction. Staff, however, has identified some on-site costs that offer the potential for city participation. Specifically, there are three public streets in the development area that have a pavement condition rating (PCR) of 0, meaning that they are in immediate need of repair and are high priorities in the public work's department's re-pavement program. Staff estimates the cost to repair these streets at $66,000.

If Council determines that public financial participation in the Montford Commons project meets its current public policy objectives, $1.3 million is the most staff can justify on a public purpose basis. This figure includes $1.0 million for acquiring the ravine, $250,000 for Traffic Signal upgrades and $66,000 for on-site street improvements of high priority city streets that currently have low Pavement Condition Ratings (PCR).

Policy Issues

It is important to note that neither RERC's suggested range of public investment nor staff's refined amount constitute a recommendation per se for the City to provide public financial support to the Montford Commons project. It is a common and generally understood aspect of being in the business of development that the developer is responsible for the cost of infrastructure and other costs made necessary by their development projects, a point that is reinforced in the City's Unified Development Ordinance (UDO) related to subdivisions:

Sec. 7-15-1(g)

(g) Street and utility construction.

(1) Plans. Construction plans for all street, water, sanitary sewer, and stormwater facilities shall be submitted to the City of Asheville concurrent with preliminary plat approval. The street and utility

construction plans for each subdivision, or portion thereof, shall include all improvements lying within or adjacent to the subdivision as well as improvements to all streets and water and sanitary sewer lines lying outside the subdivision which provide service to the subdivision. No final plat shall be approved until all improvements have been installed and approved or a guarantee accepted.

See also Section 7-11-1.

Public investment should only be considered provided that some basic policy questions are sufficiently addressed first.

Staff has identified the following basic policy questions:

1. *Does the Montford Commons Urban Village project have sufficient merits to justify consideration of a public private partnership and other means of support?*

2. "*Does this project produce significant public purpose benefits that warrant public investment when compared to other competing projects*?

3. *"Should public incentives of a $1.5 to $3.0 magnitude be used for a market-rate housing product given the absence of affordable housing units in the current project as proposed?"*

<u>Project Merits</u>
Regarding the first policy question, staff reaffirms that the Montford Commons project (as previously approved through the Planning & Zoning process) is consistent with the basic goals of the City's 2025 Plan, Smart Growth Policies, Strategic Operating plan and other official plans of the City. Specifically, it encourages infill redevelopment; proposes an efficient use of land through promotion of density; provides a walkable community within the development and into the adjacent neighborhood and to downtown; and is located on an existing bus line which supports and encourages alternative transportation options and preserves the capacity of area roadways.

<u>Public Purpose Benefits</u>
Given that other recent development projects have met the basic goals of the 2025 plan, smart growth policies and other plans without receiving public assistance for their related infrastructure costs, a second policy question emerges. That is, "*Does the Montford Commons' project provide public purpose benefits that set it apart from other worthy projects competing for public investment dollars?*" To help answer the second question, staff developed a "project scorecard" to evaluate whether the project produces enough significant and tangible public purpose benefits to make it unique. In summary, the upside of Montford Commons Phase I is that it will enhance the city and county's tax base, producing an estimated $150,000 and $180,000 annual property tax revenues for the City and County respectively; and can potentially address certain public infrastructure needs that are currently high priorities of the City. The downside, however, is that Phase I does not provide a mix of housing types, with an affordable housing component; is not likely to create many permanent jobs with desirable wages; exists outside of the City's targeted redevelopment zone; and does not develop a site that is likely to meet HUD definitions of urban blight. The full results of the "project scorecard" are provided in (Attachment A).

Affordable Housing

The most essential policy question was posed by RERC in their market feasibility and gap analysis report. That is, *"Should public incentives of this magnitude be used for a market-rate housing product given the absence of workforce/affordable housing units in the current project as proposed?"* This is a key question that Council must answer before deciding to proceed with a development agreement.

Pros:

- The project is consistent with the goals of 2025 plan and smart growth policies.
- The project provides an opportunity to develop the Montford greenway and provide connectivity to the River District.
- The project could potentially be catalytic in nature, thus spurring additional development and economic activity adjacent to and in the downtown area.
- The project could enhance the city and county property tax base.

Cons:

- The project seeks public financing in support of a housing product that does not include an affordable housing component.
- The project is outside of the City's targeted redevelopment area.
- Development of the Montford greenway is a low priority in the City's overall Greenway Master plan.
- The City is being asked to participate financially in a project that it essentially had no role in putting together. Had the City had a greater level of up-front planning (as is the case in most public/private projects), the project might have been significantly different, and met more public purposes such as affordable housing.
- The City has not provided public financial support of this magnitude to other development projects that have similar merits.

Fiscal Impact

The project is estimated to produce approximately $150,000 in annual property tax revenue for the City and $185,000 for the County. The preceding revenue is based on tax rate of $0.42 per $100 for the City and $0.525 per $100 for the County, applied to an estimated tax base of $35 million for Phase I of the Montford Commons project. (It should be noted, however, that the $35 million tax base reflects the construction value of Phase I rather than the appraised value of the project's build-out. Once the property is built out and appraised, the actual value may be more or less than the construction value.)

Annual debt service costs for a $1.3 million public investment are estimated to be approximately $170,000 per year. If the City and County participated equally in covering this cost, the city's annual debt service contribution would be $85,000, producing a net gain of $65,000 ($150,000 -$85,000) in property tax revenue for the City. The net gain, however, would likely be offset by the service impacts related to the development, as well as the costs associated with converting the ravine to a greenway.

Recommendations

If City Council determines that public assistance for the Montford Commons Project meets their current policy objectives, staff recommends that the city and county cap the public investment at a amount equivalent to an updated appraised value of the ravine, plus the cost of traffic signal upgrades, plus the city's cost to repave three on-site public streets, **or $1.3 million**, whichever is lower.

Further, if Council determines that public assistance meets there policy objectives, staff recommends that a subsequent development agreement include the following provisions:

1. City support of the project should be conditioned Frontier Syndicate demonstrating that is has contributed at least 20% equity to each phase of the project for which incentive are provided.

2. The City's financial participation is revenue-neutral. That is, the city's annual debts service costs associated with potential financing of the ravine, traffic signals upgrades and on-site city street paving of existing public streets should not exceed the annual city property tax revenue generated by the project and the cost of service impacts.

3. The City's debt service cost associated with potential participation in this project will amortized over a 10 timeframe, thus ensuring a reasonable pay-back period. A potential development agreement may also consider a 15 year time frame as needed.

4. The City and County will share the debt service costs associated the $1.3 million public investment.

5. Public participation is the project is accomplished at no risk to the City or County. That is, City and County participation will be done on a reimbursement basis following the certificates of occupancy of the vertical improvements. Land acquisition and horizontal improvements should not be started without the guaranteed delivery of completed vertical improvements and their associated fiscal revenue to the City and County.

6. Verification from the County tax office that the project will actually produce the estimated property revenues necessary to establish a revenue-neutral investment for the City and County.

7. Land acquisition costs will be based on a third-party appraisal.

8. Independent, third-party cost estimates should be completed and compared to the estimates provided by Frontier.

9. Staff structures the development agreement based on other specific provisions outlined in RERC's report.

Montford Commons Project Scorecard

Select all Applicable	Public Enhancement	Explanation for Selection/Non-selection
☐	Restoration or rehabilitation of a blighted area.	In 1987 the Montford Commons project area was deemed blighted, and CDBG investments were made in infrastructure and public improvements. While it has not been officially reclassified, city planning staff anticipates that with the new Census the characteristics will be substantially improved to the point that it no longer meets CDBG definitions of blight. Staff acknowledges, however, that the development area is currently underutilized and does not reflect the property's highest and best use, a condition that could be rectified by this project. Additionally, there is not a universal definition of what constitutes "blight"; as such, the project could qualify under other definitions of blight.
☐	Mix of housing types, including an affordable housing component consistent with housing trust fund definitions	To qualify as affordable pursuant to City Housing Trust Fund guidelines, rents must be affordable to households earning 80% or less of the median income. Montford Commons is providing a "market rate" housing product with no component that meets the preceding affordable housing guidelines.
✓	New or improved public infrastructure contiguous to the project site with a significant dollar investment in the public right-of-way.	The proposed project includes **$250,000** to **$500,000** in off-site traffic signal upgrades at the intersection of Montford Avenue and Cherry Street and Montford Avenue and Haywood Street. Improvements at these intersections are a high priority for the Transportation Department because congestion issues currently exist during the weekday morning and afternoon peak hours; thus, partnering with the developer for these improvements would produce a "general" public benefit. The proposed development site also encompasses three on-site public streets that the developer plans to repave as part of his project. The public streets in the development area currently have **pavement condition ratings** (PCR) of 0, meaning that they are in immediate need of repair and are high priorities for repair/refurbishment by the City in the near future. Staff estimates their cost to repair these streets at **$66,000**.

Select all Applicable	Public Enhancement	Explanation for Selection/Non-selection
☐	New jobs created as a direct result of the development that will remain filled for a minimum of two-years after completion of construction.	To date, specific job creation and wage data has not been provided. The Phase I residential component of the development will generate temporary construction jobs, but is not likely to create a substantial number of permanent jobs that pay wages consistent with city economic development policies.
☐	Public parking in high priority areas as designated in parking master plans.	The RERC analysis concluded that structured parking is not necessary for Phase I of the Montford Commons Project; rather, such parking is connected to the more speculative phases (II & III) of the project. Furthermore, structured parking in the Montford Commons area was not identified as a high priority in the City's 2008 Parking Master Plan.
☐	New development within a targeted redevelopment area	The City's current redevelopment focus is on underutilized areas of Central Business District (CBD). Montford Commons is on the periphery of the CBD and is thus outside of the city's targeted redevelopment area.
✓	Enhances the City's property tax base.	Phase I of the project is expected to produce approximately **$150,000** in city property tax revenue and another **$185,000** in tax revenue for the County. Note: tax revenue estimates are limited to property revenue since it is easily verifiable.
☐	Greenway development opportunities consistent with priorities outlined in greenway master plan.	The project includes the Montford greenway cooridor, which is located in the central part of the City and unites the Montford Neighborhood to the Wilma Dykeman Riverway system which is comprised of the future French Broad Greenway and Parks. The developer has requested that the City purchase and develop this cooridor for approximately **$1.0 million**. This corridor is currently a low priority in the City's overall Greenway Master Plan since the Wilma Dykeman Plan will not be implemented in the near future and the higher priority greenways provide more connectivity between other neighborhoods and destinations.